Section-By-Section for S. 984, The Fair Currency Practices Act of 2005

Background: The Exchange Rates and International Economic Policy Coordination Act of 1998 (the 1998 Act) requires that Treasury regularly make a determination of whether countries are *manipulating* the rate of exchange between their currency and the U.S. dollar for purposes of preventing effective balance of payments adjustments or gaining an unfair competitive advantage in international trade. If the Secretary of Treasury considers that such manipulation is occurring with respect to countries that (1) have material global current account surpluses; and (2) have significant bilateral trade surpluses with the United States, the Secretary is required to take action to initiate negotiations with such foreign countries on an expedited basis.

Section 1– Short Title – This Act will be known as the Fair Currency Practices Act of 2005.

Section 2– Amendments Relating to International Financial Policy

(a) – Amends the Trade Act to eliminate the necessity that a country have both a material *global* current account surplus AND a significant *bilateral* trade surplus with the United States, before the Secretary of the Treasury is required to enter into negotiations with the offending country to end its unfair practices. The change requires such negotiations if there is either a material global current account surplus OR a significant bilateral trade surplus with the United States.

Reasoning: Under current law, even if *manipulation* was found, Treasury would not be required to act unless the offending country has a significant bilateral trade surplus with the U.S. AND a material *global* current account surplus. The U.S.-China Economic and Security Review Commission recommended in its 2004 Report to Congress that the material global current account surplus condition not be required.

(b) – Amends the 1988 Act to clarify that a country engaged in "protracted large-scale intervention in one direction in the exchange market" is manipulating its currency. This language derives from the International Monetary Fund's (IMF) *Principles for Fund Surveillance Over Exchange Rate Policies*.

Reasoning: Treasury repeatedly fails to make a determination that China is manipulating its currency and the Trade Act does not specifically define *"manipulating."* This provision clarifies that a country engaged in "protracted large-scale intervention in one direction in the exchange market" is manipulating its currency. The provision does not preclude the Secretary of Treasury from finding a country to be manipulating its rate of exchange based on any other factor or combination of factors.

(c) – Requires that Treasury undertake an examination of China's trade surplus and report on its findings. The Department of Treasury should investigate why China's reported trade surplus with the U.S. and other countries differs from that reported by the trading partner countries. The report should quantify these differences so that policymakers will be better able to understand the facts behind China's trade surplus.

Reasoning: Treasury and the IMF use official Chinese statistics when determining China's global current account and trade balances. China's global current account and trade balance statistics differ markedly from the aggregate statistics of its trading partners. This results in an inaccurate depiction of China's true surplus, which is presumably much larger than reported by China. Treasury's May 2005 report to Congress once again highlighted the problems that this poses.